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**BEFORE THE ARIZONA CORPORATION C**

**COMMISSIONERS**

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BOB STUMP  
BOB BURNS  
TOM FORESE  
ANDY TOBIN

AZ CORP COMMISSION  
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Arizona Corporation Commission

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IN THE MATTER OF THE APPLICATION OF  
TUCSON ELECTRIC POWER COMPANY  
FOR APPROVAL OF ITS 2016 RENEWABLE  
ENERGY STANDARD AND TARIFF  
IMPLEMENTATION PLAN.

**DOCKET NO. E-01933A-15-0239**

IN THE MATTER OF THE APPLICATION OF  
TUCSON ELECTRIC POWER COMPANY  
FOR THE ESTABLISHMENT OF JUST AND  
REASONABLE RATES AND CHARGES  
DESIGNED TO REALIZE A REASONABLE  
RATE OF RETURN ON THE FAIR VALUE  
OF THE PROPERTIES OF TUCSON  
ELECTRIC POWER COMPANY DEVOTED  
TO ITS OPERATIONS THROUGHOUT THE  
STATE OF ARIZONA AND FOR RELATED  
APPROVALS.

**DOCKET NO. E-01933A-15-0322**

**STAFF'S CLOSING REPLY BRIEF**

The Utilities Division ("Staff") of the Arizona Corporation Commission ("Commission") responds as follows to the closing briefs filed by Tucson Electric Power ("TEP" or "Company"), the Residential Utility Consumer Office ("RUCO"), the Department of Defense ("DOD"), the Energy Freedom Coalition of America ("EFCA"), Arizonans for Electric Choice and Freeport Minerals Corporation (collectively "AECC"), Noble Americas Energy Solutions, LLC "Noble Solutions", Arizona Investment Council ("AIC"), Southwest Energy Efficiency Project ("SWEEP"), Vote Solar Initiative ("Vote Solar"), Walmart Stores Inc. and Sam's Club West Inc. (collectively "Walmart"), and Western Resource Advocates ("WRA"). The purpose of this Reply Brief is not to repeat every point made in Staff's Initial Closing Brief, nor will it attempt to refute every single issue raised by the parties listed above; instead, Staff relies upon its testimony on those issues not specifically addressed in this Reply Brief. The recommendations of Staff and its positions have been outlined in Staff's Closing Brief as well as its testimony. Staff will highlight some of the major points of disagreement

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1 with the listed parties in this brief.

2 **I. SETTLEMENT AGREEMENT.**

3 **A. Response Regarding Cost of Capital.**

4 Staff continues to recommend the adoption of the Settlement Agreement (“Agreement”). The  
5 DOD disputes the cost of capital as set forth in the agreement.<sup>1</sup> The DOD recommends a return of  
6 equity (“ROE”) with a range of 8.9 percent to 9.70 percent, with a midpoint of 9.3 percent.<sup>2</sup>

7 The ROE fair value rate of return (“FVROR”) and the capital structure are appropriate and  
8 reasonable compromises. As Company witness Ann Bulkley testified, the 9.75 percent ROE adopted  
9 in the Agreement is in line with ROEs that have been recently approved for other vertically-  
10 integrated utilities.<sup>3</sup> Even DOD witness Gorman testified that proxy companies had recently  
11 approved ROEs ranging from 9.3 percent to 10.3 percent with an average of 9.75 percent.<sup>4</sup>

12 Regarding TEP’s capital structure, DOD opposes the capital structure that was adopted in the  
13 Agreement and recommends that TEP’s actual capital structure be used.<sup>5</sup> Although Staff had  
14 originally recommended the use of TEP’s actual capital structure as of the end of the test year, the  
15 capital structure in the Agreement includes an adjustment that was known and measurable.<sup>6</sup> This  
16 TEP adjustment included the bonds in its requested capital structure because of the redemption of  
17 certain bonds that did not occur until several weeks after the test year.<sup>7</sup> TEP was legally obligated to  
18 redeem the debt during the test year and the redemption process was nearly completed by the end of  
19 the test year.<sup>8</sup> Staff believes that this was a reasonable compromise.

20 The DOD also opposes the 1.0 percent return on the fair value increment (“FVI”) of rate base  
21 included in the Agreement.<sup>9</sup> Staff witness Parcell calculated the FVI (risk free rate) to be 1.4  
22 percent<sup>10</sup> and proposed that the FVI be the midpoint between zero and 1.4 percent, i.e. .70 percent.<sup>11</sup>

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24 <sup>1</sup> DOD Br. at 2; Ex. DOD/FEA-4 at 5, 7-9 (Gorman Surebuttal).

25 <sup>2</sup> Ex. DOD/FEA-3 at 3 (Gorman Direct).

26 <sup>3</sup> Ex. TEP-12 at 4-5 (Bulkley Rejoinder); Tr. at 265:20-24.

27 <sup>4</sup> Ex. DOD/FEA-4, Ex. MPG-24.

28 <sup>5</sup> Tr. at 833:17-19.

<sup>6</sup> Ex. S-3 at 2 (Parcell Direct).

<sup>7</sup> Ex. TEP-11 at 51.

<sup>8</sup> See Ex. TEP-11 at 51; Ex. TEP-9 at 7-9 (Grant Rebuttal).

<sup>9</sup> Tr. at 835:19-25.

<sup>10</sup> Ex. S-3 at 48 (Parcell Direct).

<sup>11</sup> *Id.*

1 In its Rebuttal, TEP calculated the FVI to be 1.07 percent.<sup>12</sup> The proposed 1.0 percent FVI  
2 was a reasonable compromise and should be adopted.

3 **B. Response Regarding Energy Efficiency Program Costs In Base Rates.**

4 While SWEEP participated in the settlement discussion, SWEEP was not a signatory to the  
5 Agreement. SWEEP witness Schlegel testified that SWEEP was not a signatory because the  
6 Agreement did not resolve the issue of including energy efficiency “EE” program costs in base  
7 rates.<sup>13</sup> SWEEP proposed to add \$23 million to base rates to fund a large portion of the Company’s  
8 EE programs.<sup>14</sup> According to Mr. Schlegel, TEP has positioned EE as a core resource to meet energy  
9 needs and load growth over the next decade at the lowest cost.<sup>15</sup> SWEEP recommends that EE  
10 program costs be recovered in base rates rather than a separate adjustor mechanism.<sup>16</sup> Under the  
11 SWEEP proposal, the Commission would continue to review and approve EE programs and budgets  
12 through the Demand Side Management “DSM” Implementation Plan process. The DSM adjustor  
13 mechanism would remain, but would be used as an adjustor to recover or refund any EE funding  
14 above or below the \$23 million in base rates needed to implement Commission approved programs.<sup>17</sup>  
15 SWEEP’s similar proposal in the UNS Electric rate case was rejected by the Commission.<sup>18</sup>

16 Staff believes the program costs for EE and DSM should continue to be collected through the  
17 DSM surcharge.<sup>19</sup> By continuing with the DSM surcharge, there will be more transparency for the  
18 customer.<sup>20</sup> Staff further believes that if the program costs are included in rate base, it may take a  
19 rate case in order to exclude excess program costs.<sup>21</sup>

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24 <sup>12</sup> Tr. 262:15-24.

25 <sup>13</sup> Ex. SWEEP-2 at 2 (Schlegel Rebuttal).

26 <sup>14</sup> Ex. SWEEP-1 at 8 (Schlegel Direct).

27 <sup>15</sup> *Id.*

28 <sup>16</sup> *Id.*

<sup>17</sup> *Id.* at 9.

<sup>18</sup> Decision No. 75697 at 13 (August 18, 2016).

<sup>19</sup> Tr. at 2869:7-20.

<sup>20</sup> *Id.*

<sup>21</sup> *Id.*

1 **II. RATE DESIGN.**

2 **A. Calculation of Basic Service Charge.**

3 RUCO, EFCA, Vote Solar and SWEEP/WRA continue to oppose the Company's proposal to  
4 increase its basic service charge.<sup>22</sup> Staff continues to support the Company's proposed service charge  
5 changes. The Commission recently adopted a monthly service charge for UNS Electric that was  
6 based on the minimum system method,<sup>23</sup> the method that is under dispute in this case.

7 TEP has testified that the fixed monthly cost to serve the average residential customer is  
8 approximately \$87.<sup>24</sup> TEP argues that the basic service charge is designed to recover costs that it  
9 incurs each month, such as those for meters, billing and collection, meter reading the service line  
10 drop and other components needed to form the minimum system.<sup>25</sup>

11 According to Staff witness Solganick, the minimum system method allows for the recovery of  
12 distribution costs because those distribution assets might be needed to service peak demand.<sup>26</sup> Staff  
13 agrees that the recovery of these minimum system costs through the basic service charge is  
14 appropriate.<sup>27</sup> Moreover, Staff's long range goal is to move residential rates to a three part rate. The  
15 calculation of customer costs to be included in the basic service charge using the minimum system  
16 method advances Staff's goal.<sup>28</sup>

17 To support their position to keep the monthly service charge low, RUCO, EFCA, Vote Solar  
18 and SWEEP/WRA cite studies that show other states have either rejected an increase in service  
19 charge or ordered a service charge that was less than what was proposed.<sup>29</sup> Staff would submit that  
20 reliance on such authority is suspect since much is unknown about those utilities such as the costs to  
21 serve their average residential customer, what proportion of those costs are recovered through the  
22 fixed charge or the volumetric rate, and whether any of those utilities have declining sales volume,  
23 which leads to the under collection of fixed costs.

24 <sup>22</sup> EFCA offered testimony on this issue, but it is not clear how EFCA or its members will be impacted by the monthly  
25 service charge. When questioned, EFCA witness Garrett did not know who EFCA's members were. *See* Tr. at 2267-268.

<sup>23</sup> Decision No. 75697 (August 18, 2016).

<sup>24</sup> Ex. TEP-45 (Schedule G-6-1 at Sheet 1 of 1).

<sup>25</sup> *See* Ex. TEP-21 at 18 (Dukes Direct); Ex. TEP-28 at 7-45 (Overcast Rebuttal).

<sup>26</sup> Tr. at 2349-353.

<sup>27</sup> Ex. S-10 at 29 (Solganick Direct).

<sup>28</sup> Tr. at 2367:16-22.

<sup>29</sup> Vote Solar Br. at 10; Ex. RUCO- 10 at 10 (Huber Direct); Ex. SWEEP/WRA-2 at 7 (Baatz Surrebuttal); Ex. EFCA-9 at  
41 (Garrett Direct).

1 Both RUCO and SWEEP argue that fixed costs do not have to be collected through fixed  
2 charges.<sup>30</sup> However, as the Company has testified, its sales are declining and the increase it is  
3 proposing will only collect a portion of its fixed costs, not all of them.

4 Vote Solar and EFCA argue that an increase in the monthly service charge will act as a  
5 disincentive for customers to practice EE.<sup>31</sup> TEP provides persuasive testimony to refute these  
6 arguments. TEP witness Overcast cites to a 2012 paper by Koichiro Ito of Stanford University that  
7 found that customers respond to the total bill rather than marginal energy prices.<sup>32</sup> Dr. Overcast  
8 further testified that there is no requirement that residential customers fully understand the individual  
9 components of the rates to promote sound decisions related to a more complex rate design.<sup>33</sup>

10 EFCA witness Garret acknowledged that a greater percentage of customers respond to their  
11 total bill than don't.<sup>34</sup> RUCO also acknowledges that customers are concerned about their overall  
12 bills.<sup>35</sup> Company witness Jones concurred with such position: "In my 30 plus years of speaking with  
13 customers, I can't ever remember someone saying to me, 'What were you thinking when you  
14 changed my rates? The marginal rate has changed again!' Any time I have been fortunate enough to  
15 be able to speak with a customer, the question always revolves around their total bill."<sup>36</sup>

16 In sum, the question to be resolved isn't how many states use the basic customer method or  
17 minimum system method to determine the monthly fixed charge. What must be determined is the  
18 appropriate balance between recovery of fixed costs and how to fashion rate design to allow TEP, in  
19 its unique circumstance, to recover costs it incurs to serve its customers when it can no longer rely on  
20 the volumetric component to recoup a portion those costs. Staff is comfortable with TEP's approach  
21 to developing its monthly service charges and recommends their adoption by the Commission.

## 22 **B. Walmart Revenue Rider.**

23 To address a portion of the inter-class subsidies reflected in the Class Cost of Service Study  
24 ("CCOSS"), Walmart has suggested the use of a rate support rider. Walmart's subsidy mitigation  
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26 <sup>30</sup> SWEEP Br. at 10; RUCO Br. at 16.

27 <sup>31</sup> Vote Solar Br. at 19.

28 <sup>32</sup> Ex. TEP-28 at 93 (Overcast Rebuttal).

<sup>33</sup> *Id.*

<sup>34</sup> Tr. at 2279:18-20.

<sup>35</sup> Ex. RUCO-11 at 41 (Huber Surrebuttal).

<sup>36</sup> Ex. TEP-32 at 16 (Jones Rejoinder).

1 plan would eliminate the subsidies paid by commercial and industrial classes over eight years.<sup>37</sup>  
2 Such proposal would increase residential bills every year for eight years.<sup>38</sup>

3 Staff witness Solganick expressed some reservations about Walmart's plan, stating that one of  
4 Staff's concerns was that the rider presumed that the relative positions of the customer classes (the  
5 subsidy) would not change over that period due to increased DG penetration, EE or opening or  
6 closing of new accounts (residential, commercial, industrial and governmental).<sup>39</sup> Additionally, the  
7 rider fails to take into account that sales over the next eight years will be different from the Test  
8 Year.<sup>40</sup> Given this, Mr. Solganick opined that an adjustment and reconciliation methodology and  
9 Plan of Administration must be developed at the implementation of the plan and that the Commission  
10 should not move forward on this concept without a detailed debate and understanding of its effects  
11 and supposed benefits.<sup>41</sup>

### 12 C. Economic Development Rider.

13 TEP proposes an Economic Development Rider ("EDR") that is intended to attract new jobs  
14 and economic activity. The EDR is similar to the EDR that was recently approved for UNS Electric.  
15 The EDR will provide a discount to customer that qualify under existing Arizona economic  
16 development tax credits.<sup>42</sup> To qualify customers must have a minimum load factor of 75% and have  
17 a peak demand of at least 3,000 kW.<sup>43</sup> The discount would be phased out over five years.<sup>44</sup> The  
18 proposed discount is higher for customers that "infill" in areas with existing facilities.<sup>45</sup>

19 Staff believes the proposed EDR has limits and is biased towards existing facilities.<sup>46</sup> Staff is  
20 also concerned that combining the proposed EDR rate with the proposal to include generation within  
21 the Lost Fixed Cost Recovery ("LFCR") mechanism may have unintended consequences.<sup>47</sup> Mr.  
22 Solganick posits that the Company could bill existing customers for the generation costs within the  
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24 <sup>37</sup> Ex. Walmart-2 at 15.

<sup>38</sup> Tr. at 1832:9-13.

25 <sup>39</sup> Ex. S-12 at 25 (Solganick Surrebuttal).

<sup>40</sup> *Id.*

26 <sup>41</sup> *Id.*

<sup>42</sup> Ex. TEP-21 at 31-32 (Dukes Direct); Ex. S-10 at 49 (Solganick Direct).

27 <sup>43</sup> Tr. at 1376:4-13.

<sup>44</sup> *Id.*

<sup>45</sup> *Id.*

28 <sup>46</sup> Ex.S-10 at 51 (Solganick Direct).

<sup>47</sup> *Id.* at 55.

1 LFCR mechanism, redirect the generation (energy and capacity) to a new customer attracted by the  
2 EDR and effectively double collect on that load.<sup>48</sup>

3 In the event that the energy costs are not significant, then Staff would support this limited  
4 (volume and time) program to increase employment in TEP's service territory. Staff's support for the  
5 program does not extend to a Company request for recoupment of lost incremental revenues absent a  
6 supporting record in some future proceeding.<sup>49</sup>

### 7 **III. THE BUY-THROUGH PROPOSALS SHOULD BE REJECTED.**

8 Staff, in general, agrees with TEP's and AIC's assessment regarding the merits, but not with  
9 their arguments regarding the legality of the buy-through proposals in this case. Staff has no  
10 opposition to approval of a buy-through rate provided there are no adverse impacts and no costs to all  
11 other customers.<sup>50</sup> However, none of the buy-through options being proposed offer that assurance.  
12 As noted by Staff, the proposed buy-through programs choose winners and losers in the business  
13 community.<sup>51</sup> Under each of the proposals, customers not lucky enough to be chosen for the buy-  
14 through rate will end up covering the fixed costs that would have otherwise been covered by the  
15 customers that are selected.<sup>52</sup>

16 Further, Staff shares RUCO's concern that other classes of customers, including the  
17 residential class, may also be harmed by these buy-through proposals.<sup>53</sup> While Arizona Public  
18 Service ("APS") currently has a buy-through tariff ("AG-1"), it is important to note that it was agreed  
19 to as part of a global settlement, and that APS, in return for other concessions, agreed not to seek  
20 recovery of unmitigated lost fixed generation costs associated with its AG-1 tariff from residential  
21 customers.<sup>54</sup> This is not the case with TEP. Although TEP entered into a partial settlement with a  
22 number of parties regarding revenue requirement, it did not include its ER-14 tariff. As such, TEP  
23 would be entitled seek recovery of any lost fixed generation costs associated with the adoption of a  
24 buy-through rate.

25 \_\_\_\_\_  
26 <sup>48</sup> *Id.*

27 <sup>49</sup> *Id.* at 51.

28 <sup>50</sup> Ex. S-10 at 47.

<sup>51</sup> Ex. S-12 at 21:6-7.

<sup>52</sup> *Id.* at 21:25-26.

<sup>53</sup> RUCO Br. at 23.

<sup>54</sup> Decision No. 73183 at Ex. A, Section 17.2 (Settlement Agreement).

1 Both AIC and TEP assert that all of the buy-through proposals are unconstitutional.<sup>55</sup> Staff  
2 disagrees with this assertion. As noted by AIC, the Commission has “plenary” power over utility  
3 ratemaking, and it must ascertain the fair value of the property within the state of every public service  
4 company doing business within the state. It is AIC’s and TEP’s contention that all of the buy-  
5 through proposals in this case fly in the face of these requirements. In making this assertion, they  
6 rely primarily on *Phelps Dodge Corp. v. Arizona Elec. Power Co-op.* wherein the Court indicated  
7 that while market forces may influence the Commission’s determination of what rates are “just and  
8 reasonable,” the Commission cannot abdicate its constitutional responsibility to set just and  
9 reasonable rates by allowing competitive market forces alone to do so.<sup>56</sup>

10 It is also AIC’s and TEP’s assertion that the operation of the buy-through proposals in this  
11 case is illegal for two primary reasons. First, it improperly delegates to the competitive market place  
12 the Commission’s duty to set just and reasonable rates that provide for the needs of all whose  
13 interests are involved, including public service corporations and the consuming public. Second, they  
14 assert that the proposals violate the Constitutional requirement that rates include consideration of the  
15 fair value of the public service corporation’s property.<sup>57</sup>

16 TEP was required to present a buy-through proposal in this case as a result of the Settlement  
17 Agreement reached and approved in Decision No. 74689. Although that decision does not specify  
18 what that buy-through proposal must include, other than it be available to large light and power and  
19 large power service customers, it appears TEP’s proposal was modeled largely on APS’ AG-1  
20 experimental pilot program in all material aspects except one. Unlike TEP’s proposal, and seemingly  
21 the other proposals in this case, the AG-1 rate includes a minimum and maximum range whereby the  
22 buy-through rate can operate that the Commission determined was “just and reasonable”.<sup>58</sup>

23 The Court in *Phelps Dodge* specifically determined that if the Commission establishes a range  
24 of rates that is “just and reasonable,” the Commission does not violate article 15, section 3 of the  
25 Arizona Constitution by permitting competitive market forces to set specific rates within that  
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27 <sup>55</sup> AIC Br. at 5, TEP Br. at 45.  
28 <sup>56</sup> 207 Ariz. 95, 107 (2004).  
<sup>57</sup> TEP Br. at 45, AIC Br. at 6.  
<sup>58</sup> Decision No. 73183.

1 approved range.<sup>59</sup> It is perplexing that TEP submitted a buy-through proposal in this this case that  
2 omitted a key feature of APS' AG-1 tariff, and then asserts that it is unconstitutional because of its  
3 absence. Importantly, to the extent the Commission is inclined to authorize a buy-through tariff in  
4 this instance, which Staff is not recommending for substantive reasons,<sup>60</sup> this problem is easily  
5 remedied by the existing record. The Commission could simply incorporate the rates structure from  
6 the APS AG-1 tariff into TEP's ER-14 rate. Staff believes this would cure any shortcomings.

7 The other issue is that of "fair value." TEP and AIC essentially argue that the buy-through  
8 proposals ignore "fair value."<sup>61</sup> This is incorrect. An important attribute of the buy-through  
9 proposals in this case is that TEP actually takes title to the power that is being procured. If an upper  
10 and lower limit for the rate is set by the Commission in this case, then the "fair value" finding will  
11 satisfy article 15, section 14 of the Arizona Constitution. Thus, the Commission will have  
12 determined the fair value of the Arizona property owned by TEP, and that value will presumably be  
13 considered in setting the range of rates for any buy-through proposal. In other words, since TEP  
14 would be taking title to the power as part of this process, the "fair value" that must be determined is  
15 that of TEP, and not that of whomever TEP may be procuring power from on behalf of the ER-14  
16 customer.

17 Even without the inclusion of a range as discussed above, the buy-through proposals in this  
18 case are akin to an adjustor mechanism or a formula rate, both of which are permissible. In  
19 particular, TEP, UNSE, and APS currently have mechanisms in place that incorporate a pass-through  
20 element that is directly passed through to customers. One example of these is APS' Transmission  
21 Cost Adjustment that recovers transmission costs associated with serving retail customers at an  
22 amount approved by the Federal Energy Regulatory Commission.<sup>62</sup> Another is UNS Electric's  
23 Purchased Power and Fuel Adjustment Clause that facilitates a pass-through to customers of a  
24 forward looking estimate of fuel and purchased power costs.<sup>63</sup> In other words, Staff believes that  
25 these pass-through proposals also fit the mold of an adjustor mechanism or a formula rate.

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27 <sup>59</sup> 207 Ariz. 95, 109.

28 <sup>60</sup> See Staff's Br. at 18-24.

<sup>61</sup> TEP Br. at 46; AIC Br. at 9.

<sup>62</sup> See Decision No. 73183.

<sup>63</sup> E-04204A- 06-0783, Notice of Filing Revise Purchased Power and Fuel Adjustment Clause POA. (June 26, 2008).

1           **A.     AECC and Noble Solutions.**

2           It is not altogether clear what AECC and Noble Solutions are seeking within the confines of  
3 this case. They assert that “there are no legal impediments that prohibit the Commission from  
4 implementing competition in electric generation, or adopting any of the alternative generation service  
5 programs proposed by AECC and Noble Solutions in this proceeding.<sup>64</sup> AECC and Noble rely on  
6 A.R.S. § 40-202(B) in support of their recommendation.

7           This statute reads in part: “[i]t is the public policy of this state that a competitive market shall  
8 exist in the sale of electric generation service.”<sup>65</sup> To the extent AECC and Noble Solutions are  
9 advocating for the implementation of competition in generation for *public service corporations*, it is  
10 hard to overlook the Court’s ruling in *Phelps Dodge* wherein the Court specifically indicated that “the  
11 Commission cannot carry out its constitutional mandate by allowing competitive market forces to  
12 exclusively determine what is “just and reasonable.”<sup>66</sup> In other words, true market rates do not pass  
13 constitutional muster. On the other hand, AECC and Noble are suggesting the buy-through  
14 proposals in this case are legal, Staff agrees that they could be legal if the Commission were to set a  
15 range within which the buy-through rates were required to operate, as discussed above.

16           **B.     The Buy-Through Proposals Do Not Violate The Interference With Management**  
17           **Doctrine.**

18           TEP argues that the buy-through proposals offered in this case tread on the utility’s  
19 prerogative to determine what mix of generation to acquire and therefore, impermissibly interferes  
20 with the management of the Company.<sup>67</sup> TEP essentially asserts that the Commission has historically  
21 acknowledged that it is the electric utility’s obligation to acquire a prudent mix of generation and that  
22 the Commission, after the fact, simply evaluates the prudence of those decision. That is simply not  
23 the case.

24           The Commission, in the exercise of its regulatory power, may interfere with the management  
25 of public utilities whenever the public interest demands.<sup>68</sup> In fact, the Arizona Court of Appeals

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27 <sup>64</sup> AECC/Noble Br. at 32.

<sup>65</sup> A.R.S. § 40-202(B).

<sup>66</sup> 207 Ariz. 95, 129 ¶153.

<sup>67</sup> TEP Br. at 47.

<sup>68</sup> *Southern Pacific Co. v. Arizona Corp. Comm’n*, 98 Ariz. 339, 343 (1965).

1 recognized that within the context of resource mix, “[p]rophylactic measures designed to prevent  
2 adverse effects on ratepayers due to a failure to diversify electrical energy sources fall within the  
3 Commission's power ‘to lock the barn door before the horse escapes `.’”<sup>69</sup> Just as it was within the  
4 Commission’s authority to require electric utilities to diversify their generation portfolios through the  
5 REST rules, if the Commission were to approve an appropriate buy-through tariff (not something  
6 Staff is recommending) so too would it fall within the Commission’s authority to do so.

7 **C. Staff Does Not Support Freeport’s Franchise Agreement.**

8 Freeport is proposing that TEP enter into a franchise agreement with Morenci Water &  
9 Electric (“MWE”), which is owned by Freeport.<sup>70</sup> The proposed franchise agreement is similar to the  
10 one between MWE and Graham County Electric Cooperative, Inc. (“Graham”) approved by the  
11 Commission in 2006.<sup>71</sup> That arrangement involved the development of a mine at Safford, Arizona,  
12 by PD Safford. This mine was located in Graham's service area and the parties entered into a Service  
13 Territory Franchise Agreement (“STFA”) which enabled MWE to provide power to PD Safford for  
14 its mining operations. Under Freeport’s proposal, MWE would take over electric service to the  
15 mine.<sup>72</sup>

16 Under the STFA, Graham was a willing participant. In this instance, however TEP has not  
17 agreed to the arrangement.<sup>73</sup> As Freeport witness McElrath acknowledged, TEP is ready and willing  
18 to serve.<sup>74</sup> Mr. McElrath also acknowledges that the Sierrita operations are not in danger of shutting  
19 down if a Franchise Agreement is not entered into with TEP.<sup>75</sup>

20 Without the voluntary agreement of TEP, it may be difficult to force TEP into such an  
21 arrangement. TEP has the CC&N to serve the Sierrita mine. Unless the public interest is served by  
22 disregarding TEP’s exclusive right to serve in its CC&N area, there may not be grounds to compel  
23 TEP to enter into an agreement with MWE.<sup>76</sup>

24 \_\_\_\_\_  
25 <sup>69</sup> *Miller v. Arizona Corp. Comm'n*, 227 Ariz. 21, 29, ¶ 31, 251 P.3d 400, 408 (App. 2011).

26 <sup>70</sup> See Tr. at 1713:20-25.

27 <sup>71</sup> Decision No. 69211 (December 21, 2006).

28 <sup>72</sup> Ex. AECC-14 at 11-13 (McElrath Surrebuttal).

<sup>73</sup> Tr. at 1730:14-16.

<sup>74</sup> *Id.* at 1730:20-25.

<sup>75</sup> Tr. at 1737:8-20.

<sup>76</sup> *James P. Paul Water Co. v. Ariz. Corp Comm'n*, 137 Ariz. 426, 429, 671 P.2d 404, 407 (the Commission may alter or delete a CC&N only where the holder is unable or unwilling to provide reasonable service at a reasonable price.)

1 **IV. TORS PROGRAM.**

2 In its Opening Brief, EFCA takes issue with the fact that Staff did not conduct a prudency  
3 review of TEP's TORS program as it asserts was required by the Commission in Decision No.  
4 74884.<sup>77</sup> EFCA contends that, based on this omission and the testimony presented, the TORS pilot  
5 program was not cost effective, was completely unnecessary and should not be rate based.<sup>78</sup> As ever,  
6 EFCA sets forth in its argument only those assertions that serve its purposes and neglects to include  
7 all facts relevant to the issue.

8 In point of fact, Staff does not dispute that Decision No. 74884 provides that a determination  
9 of prudency of the TORS pilot program "will be made during the rate case in which TEP requests  
10 cost recovery of this project."<sup>79</sup> However, significantly, EFCA acknowledges that "the scope of a  
11 prudency review is determined on a case-by-case basis and can include various types of actions  
12 including, without limitation, "a determination of whether everything is working as it should;...[a]  
13 determination of the existence of cost overruns or inefficiencies; and project-specific inquiries."<sup>80</sup> As  
14 Staff witness, Michael McGarry, similarly explained, "[p]rudency is a determination of whether or  
15 not what was being spent, what actions that management has taken that has resulted in costs that were  
16 either inefficient and/or unnecessary"<sup>81</sup> According to Mr. McGarry, there is no general checklist,  
17 yardstick, guide or set of rules for conducting a prudency review; it depends on the subject matter.<sup>82</sup>

18 In this instance, what EFCA fails to note in its criticism of Staff is that the amount of the  
19 TORS program presently installed and sought to be included in rate base and, thereby, would be  
20 subject to a prudency review is only \$16,641 of a total \$10 million.<sup>83</sup> Staff submits that a prudency  
21 review does not involve the evaluation of a utility's every asset and, in this case would equate to the  
22 review of 0.0016 percent of the entire proposed program. Staff further submits that, under EFCA's  
23 acknowledged case-by-case standard, engaging in such a costly endeavor in light of the limited  
24 amount of the program presently installed would be equally, if not more, imprudent. In addition,

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26 <sup>77</sup> EFCA Br. at 20:11-13.

<sup>78</sup> *Id.* at 21:3-5.

<sup>79</sup> Decision No. 74884 at 21:16-20.

<sup>80</sup> EFCA Br. at 20:18-23.

<sup>81</sup> Tr. at 1952:8-11.

<sup>82</sup> *Id.* at 1952:18-22; 1953:9-10.

<sup>83</sup> Tr. at 2856:20 - 2857:4; TEP Response to STF DR 25.4, see Attach. A.

1 Staff would suggest that conducting a prudency review on such a minute portion of the proposed  
2 TORS program would not elicit a true determination of whether the actions taken by TEP  
3 management resulted in inefficient and/or unnecessary costs.

4       Elijah Abinah, Assistant Director of the Commission's Utility Division, testified that  
5 conducting a prudency review on such an insignificant portion of the program would be "wasting the  
6 Commission resources" which would be quickly pointed out by the likes of EFCA.<sup>84</sup> Mr. Abinah  
7 further testified that "at the appropriate time [Staff] would do the prudency review and make the  
8 recommendations of the Commission of the \$10 million" and not "waste the Commission's resources  
9 and money to do [a] \$16,000 prudency review...."<sup>85</sup> Staff believes that, once the program is more  
10 fully installed, a prudency review would better serve its purpose and enable the Commission to  
11 determine whether "everything is working as it should" and/or determine the existence of cost  
12 overruns or inefficiencies. Staff submits that the lack of a prudency review of the \$16,641 installed  
13 TORS program should not prevent its inclusion in rate base under the present circumstances.  
14 EFCA's recommendation becomes even more absurd given the fact that TEP has a FVRB of  
15 \$2,843,985,854 and that the TORS program is a pilot program that the Commission to approved in  
16 Decision No. 74884 with the significant reporting requirement that will allow Staff and ultimately the  
17 Commission to evaluate this program and determine whether it should be continued.

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28 <sup>84</sup> Tr. at 2857:1-21.

<sup>85</sup> Tr. at 2858:8-13.

1 **V. CONCLUSION.**

2 For the reasons discussed above, in Staff's Closing Brief, and the record in these consolidated  
3 matters, Staff recommends approval of the Settlement Agreement and adoption of Staff's positions  
4 regarding the remaining issues in this case.

5 RESPECTFULLY SUBMITTED this 14<sup>th</sup> day of November, 2016.

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18 On this 14th day of November, 2016, the foregoing document was filed with Docket Control  
19 as an Utilities Division Brief, and copies of the foregoing were mailed on behalf of the Utilities  
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